National Association of Home Builders

Housing Finance & Regulatory Affairs
Jessica R. Lynch
Vice President, Housing Finance
jlynch@nahb.org

May 17, 2023

The Honorable Sandra Thompson
Director
Federal Housing Finance Agency
Office of the Director
400 7th Street, S.W.
10th Floor
Washington, D.C. 20219

Re: Enterprise Single-Family Social Bond Policy
Request for Input

Submitted via email to: https://www.fhfa.gov/AboutUs/Contact/Pages/Request-for-Information-Form.aspx

Dear Director Thompson:

On behalf of the National Association of Home Builders of the United States (NAHB), I welcome the opportunity to submit comments to the Federal Housing Finance Agency (FHFA) regarding the request for input on Fannie Mae's and Freddie Mac's single-family social bond policy and program design. While both organizations, (together, "the Enterprises,") have issued "labeled" multifamily social bonds with specific criteria evaluated by an independent third party, neither has issued a single-family bond specifically designated as a social bond. We appreciate FHFA's efforts to seek input on the single-family social bond frameworks developed to-date by the Enterprises and consider thoughts and recommendations for future actions to issue single-family social bonds attractive to investors due to having increased transparency and widely recognized social characteristics and objectives.

NAHB is a Washington, D.C.-based trade association representing more than 140,000 members involved in the development and construction of for-sale single-family homes, including homes for first-time and low- and moderate-income home buyers, as well as the construction, ownership and management of multifamily rental housing, including affordable rental housing. The ability of the home building industry to meet the demand for housing, including addressing affordable housing needs, and significantly contribute to the nation's economic growth is dependent on an efficiently operating housing finance system. The nation's housing finance system must offer home buyers in all geographic areas access to affordable mortgage financing at reasonable interest rates through all economic conditions and provide financing for multifamily housing development to support affordable rental opportunities.

Background

The consideration of Environmental, Social, and Governance (ESG) concerns has become increasingly significant and prevalent in the finance arena. Within the ESG framework, bond issuers have structured transactions designed to finance the various environmental, social and governance causes that investors want to support. Both Fannie Mae and Freddie Mac have developed frameworks for issuing mortgage-backed securities (MBS) and corporate bonds to meet ESG interests. The Enterprises have designed affordable and green mortgage loan products that meet specific environmental and social goals. These loans collateralize MBS and the proceeds from sales of the MBS, as well as proceeds from specifically designated corporate bonds, finance ongoing green and social objectives.

Both Freddie Mac and Fannie Mae currently are issuing a variety of "labeled" multifamily mortgage bonds that fall under the broad rubric of ESG securities. Their labeled multifamily bonds include Social, Green and Sustainable Bonds that satisfy criteria developed by the International Capital Markets Association (ICMA.) ICMA defines Social Bonds as bond instruments that finance or refinance new or existing social projects and align with ICMA's Social Bond Principles. The ICMA Principles provide guidelines for best practices for the issuance of labeled bonds, but adherence to these guidelines is voluntary and the principles are not comprehensive.

Also, both Fannie Mae and Freddie Mac create, issue and disclose single-family MBS that would be considered by some as social bonds due to their collateralization by mortgages originated under the Enterprises' single-family affordable mortgage loan product guidelines. However, these MBS are not "labeled" social bonds because they lack the standardization confirmed by an industry-endorsed framework that includes monitoring and reporting on the use of proceeds to validate the social impact of the underlying mortgage loan collateral. While these MBS sometimes generate pay-ups over to-be-announced (TBA) MBS, pay ups may not be consistent depending on the investor's confidence in understanding the underlying collateral. Understanding the collateral is important for two reasons: an investor in a social bond wants to know the bond meets the social target the investor is seeking and pay ups are determined by the prepayment expectations of the bond, which are determined by the specific social characteristics of the underlying collateral. The Enterprises' affordable mortgage loan collateral tends to prepay more slowly than other products, which is why an investor generally will pay up for MBS backed by these mortgage loans.

The standardization provided by an industry-endorsed social bond protocol eliminates the need for an investor to perform much of its own due diligence on the underlying mortgage collateral and provides an investor with enough disclosure of the social characteristics of the collateral to assure an investor the bond can be deemed or "labeled" a social bond. Social bonds are considered "specified" or "spec" bonds because investors are seeking specified collateral, for which they are willing to pay a better price.

FHFA soliciting input on whether Enterprise-issued labeled social bonds will incent investment in these pools and generate proceeds to fund additional acquisitions by the Enterprises of mortgage loans that promote sustainability, affordability and equity in homeownership. As importantly, FHFA asks who should benefit from potential pay ups for these social bonds? If pay ups accrue to lenders, can they ensure increased incentive for lenders to originate loans eligible for social bonds, thereby increasing the availability of mission-oriented loans to home buyers and homeowners? Will lenders pass pricing benefits to homebuyers and homeowners? Is increased availability of financing enough of a benefit to homeowners and homebuyers?

<u>Current Fannie Mae and Freddie Mac Single-Family Social Bond Criteria</u>

Freddie Mac issues single-family affordable MBS pools collateralized by mortgage loans to borrowers using the Enterprise's affordable mortgage lending products or loans on manufactured homes targeting very low-, low-, and moderate-income borrowers. The proceeds of these MBS bonds are used to purchase or refinance additional mortgage loans meeting the specific eligibility requirements for inclusion in an affordable MBS bond.

Fannie Mae also issues single-family sustainable MBS collateralized by mortgage loans to borrowers meeting specified eligibility criteria. The proceeds from the sale of Fannie Mae's single-family sustainable MBS finance the acquisition or refinancing of a property that must meet one of the eligibility criteria for inclusion in the sustainable MBS. Fannie Mae's list of eligible criteria includes supporting financing for vulnerable groups such as those impacted by natural disaster, enabling the acquisition or financing of single-family housing in underserved communities, providing access to capital to traditionally underserved and underrepresented groups, enabling the acquisition or financing of single-family housing affordable to low- to moderate-income individuals and families using the Area Median Income (AMI) designations of very low-income, low-income, moderate-income and workforce housing.

Recently, both Fannie Mae and Freddie Mac have taken steps toward "labeling" single-family MBS pools as social bonds by developing a Social Index. The Social Index is a disclosure comprised of two scores that are disclosed to investors to help them identify single-family MBS pools with greater concentrations of loans possessing certain "social" characteristics at the time of pool formation. The two scores making up the Social Index are the Social Criteria Share and the Social Density Score.

The investors see the two scores and are able to judge whether their investment would support low-income borrowers, underserved minorities, first-time homebuyers or mortgages on manufactured housing, homes in low-income areas, minority tracts, high needs rural areas, or designated disaster areas and note the relative concentrations of each in the pool. With this method of disclosure, the Enterprises have tried to balance meaningful transparent disclosure of the social benefits of the MBS with concerns of protecting the privacy of individual borrowers.

NAHB Comments

Social bonds are described broadly as intended to generate proceeds to improve a societal problem afflicting a group of people most vulnerable. The social issues of affordable housing, access to housing, housing and financial equity, and the racial wealth gap caused, in part, by unequal access to homeownership, all appear to lend themselves to benefit from the general objective of a social bond issuance. At the direction of FHFA and through Duty to Serve, Equitable Housing Plans and affordable housing goals, Fannie Mae and Freddie Mac are expanding efforts to address these societal concerns through various lending policies, mortgage programs and products, and regulatory and charter mandates.

It is critical the Enterprises and FHFA balance their efforts to address these societal concerns with efforts to advance the Enterprises' overarching mission to provide liquidity and stability to the mortgage market while ensuring they operate in a safe and sound manner. NAHB members' businesses are sensitive to changes in interest rates and any disruptions to the housing finance system that would impact the availability of mortgage credit. The effective functioning of the TBA market should be at the forefront as FHFA considers a social bond structure. Any effort to create social bonds should not be at the expense of providing liquidity to the broader market.

If a labeled social bond can generate consistent and somewhat predictable pay ups for lenders that ultimately benefit home buyers and homeowners that would be a positive social impact – whether homeowners and home buyers benefit from better pricing or increased availability of the Enterprises' affordable products and programs. If, ultimately, too many specified pools are created to the detriment of the liquidity of the regular TBA market that would be a negative impact. FHFA should thoroughly analyze the data and consider these impacts in determining if a labeled social bond is more advantageous in the long term than the Enterprises' current Social Index disclosure system.

Response to Specific Questions

Question A-1: What program outcomes and borrower impacts should an Enterprise Single--Family Social Bond program seek to achieve? Which borrower benefit impact measures should be reported?

A single-family labeled social bond program should generate enough increased investor interest to issue specified pools on a consistent basis with pay-ups that are more reliable and greater than those of the bonds issued currently that are backed by the Enterprises' affordable mortgage loan products. The impact measures should include the pay up attributed to the social bond label, and whether lenders are increasing their originations and sales of additional mission-centric mortgage loans to the Enterprises.

In addition, any benefits that accrue to home buyers and homeowners should be clearly defined, monitored and reported.

Question A-4: Should the Enterprises isolate, measure, and report on increased market liquidity for Enterprise social bonds and any resulting benefit for eligible borrowers? If so, how?

Yes, if FHFA directs Fannie Mae and Freddie Mac to move forward with a labeled social bond, the Enterprises should isolate, measure, and report on increased market liquidity for Enterprise social bonds and any resulting benefit for eligible borrowers. Together with the investor community and industry stakeholders, FHFA and the Enterprises should agree on a new protocol, or follow ICMA's Social Bond Principles, to isolate, measure and report on whether labeled social bonds are generating proceeds above those that are generated on regular agency MBS and current specified pools. FHFA and the Enterprises also should closely monitor the impact of the labeled social bonds on the overall housing finance system, borrower privacy and market liquidity.

A labeled social bond policy should include a requirement for transparent reporting of the impact of labeled social bonds and such reporting should not be overly burdensome or costly for lenders or the Enterprises.

The Enterprises and FHFA should work with the investor community to create disclosures that meet investors' needs for evaluating a social bond while also protecting the privacy of individual borrowers.

Question B-1: What attributes should be used to determine whether a loan is eligible for a social bond pool (e.g., income, geography, down payment assistance, reduction in mortgage interest rate, buydown programs)?

The determination of whether a loan is eligible for a social bond pool should be whether its attributes make it eligible for one of Fannie Mae's and Freddie Mac's affordable loan products that is active at the time and/or qualifies under one of the Enterprises' housing goals, i.e. low-income home purchase, very low-income home purchase, low-income refinance, minority census tract, low-income census tract, or meets criteria in the Enterprises' Duty to Serve plans. If the Enterprises purchase loans identified by lenders as originated within a Special Purpose Credit Program loans, they also should be considered eligible for a social bond pool that has the applicable characteristics.

Please contact Rebecca Froass at rfroass@nahb.org for additional information or to answer any questions you may have regarding these comments.

Sincerely,

Jessica R Lynch

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